

# Debt-for-Diploma System

Student-loan debt saddles college grads long after they earn degrees

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**O**ver the past several decades, college tuition has nearly tripled, adjusting for inflation, and federal student aid has shifted from a predominantly grant-based system to one dominated by loan aid. These two factors have conspired to create a debt-for-diploma system, affecting young adults' choices about college, including where they enroll and whether or not they complete degrees. With two out of three undergraduates leaving school with student loan debt averaging \$19,300, the debt-for-diploma system also exerts a powerful influence on young people's financial stability long after they've received their degrees.

Financial barriers represent a formidable obstacle for college enrollment and completion. For nontraditional students, the ability to afford college includes being able to pay for classes, books and basic living expenses such as transportation, rent, utilities and groceries. In order to meet both the direct and indirect expenses of college, many lower-income students are working more hours than is conducive to academic study. The Denver-based Education Commission of the States and the League for Innovation in the Community College found that 48% of community college undergraduates work at jobs in order to support their education. The U.S. Department of Education reports that nearly three-quarters of today's full-time college students hold down jobs, nearly half of them working 25 hours or more a week.

Students are working longer hours, accumulating unprecedented amounts of debt and taking longer to graduate in order to close the gap between the costs of college and financial aid. This unmet need is particularly great for lower-income students. In 1999-2000, the average community college student receiving a Pell Grant still had unmet need of more than \$3,000 after all aid

was taken into account, according to a report by MDRC. U.S. Education Department data reveal that a public college student from a family with an annual household income of \$62,240 or less will have an average of \$3,600 in annual unmet need, while students from families with an annual household income of \$34,288 or less will have average annual unmet need of \$4,689.

The gap between grant aid and the cost of attending college isn't too surprising considering the disproportionate amount of federal aid spent on loans or tax credits — forms of student aid that least influence the enrollment decisions of lower-income and first-generation college students. According to the College Board, of the \$94 billion spent on federal student aid in the 2005-06 school year, only \$18 billion was for grant aid, while loan-based aid comprised more than \$68 billion, and tax credits \$6 billion. Not only do grants comprise a smaller share of federal financial aid, but their purchasing power has declined precipitously, failing to keep pace with the cost of tuition and the surge in eligible students.

The federal government has failed to maintain funding levels for Pell Grants, which were originally intended to cover 75% of the cost of going to college for low- and moderate-income students. The maximum Pell Grant today covers about one-third of the cost of a four-year college. And only 22% of Pell recipients get the maximum; the average award in 2006 was \$2,354, which covers less than half the average tuition and fees at public universities. The Project on Student Debt reports that 88% of Pell recipients now borrow, compared with 52% of their non-Pell counterparts, and borrow at higher amounts.

As costs have risen and grant aid has become anemic, students are being denied access to postsecondary

education because it is unaffordable. The federal Advisory Committee on Student Financial Assistance estimates that if current trends continue, by the end of the decade, 4.4 million college-qualified students will not attend a four-year college and 2 million will not attend college at all because they cannot afford it.

Once enrolled, many students find the financial challenges overwhelming. Community college students cite financial factors as a main reason for quitting their studies. The financial challenges often mean young people churn in and out of college, taking time off so they can work full-time to amass the money needed to pay for tuition, books and other school expenses. Too many never find their way back to campus, as the pull of a paycheck is greater than the pull of college studies. Many of these young people join the one in five student borrowers who start out trying to get an education and minimize the expense for themselves, but end up with the worst of all possible results: debt and no diploma.

The cost burden is also substantial for traditional, four-year college students from low-income backgrounds. Since 1980, tuition at public four-year universities has more than doubled, after adjusting for inflation. In 2006, the average tuition at a public four-year college was \$5,836, up from \$2,628 in 1986 (2006 dollars), according to the College Board. Add in room and board charges for four-year colleges, and the total cost of attending in 2006 was \$12,796, up from \$7,528 in 1986. After adjusting for inflation, the average cost to attend a state university today is equivalent to what it cost to attend a private university a generation ago.

Higher tuition and dwindling financial aid mean most college students now borrow to pay for school. Some argue that the economic benefit a college degree commands in the labor market

justifies incurring more student loan debt. While it is true that someone with a bachelor's degree will earn approximately \$1 million more over a lifetime than someone without a college degree, it is also true that the earnings for male college graduates have remained flat for three decades, while women with bachelor's degrees today earn only about 10% more than their mothers did a generation ago and \$8,900 less per year than college-educated young men. Earnings for young workers with "some college" have declined, with the typical young male worker with "some college" earning 21% less than the previous generation and similarly educated young women earning 6% less.

A survey by the lender Nellie Mae finds that young adults who had been paying back their loans for at least three years reported feeling *more* burdened than those who were in their first years of repayment, and less likely to agree that the benefits of a

college degree made the debt worthwhile. This is counterintuitive because one could reasonably assume that as young college grads' salaries rise and student debt takes up less of the monthly paycheck, the debt would feel like less of a burden.

One reason student loan debt may feel more burdensome as graduation is further in the rearview mirror could be the drag that loan payments have on a young person's ability to get ahead financially. Research by Demos has found that young college-educated households led by 18-to-34-year-olds carrying education-related debt had median financial assets that were 28% lower than college-educated households without student debt. Only 6% of young adult households with education debt would have enough financial assets to sustain them for three months if they lost their primary source of income, compared with 22% of those without education debt.

After years of unresponsiveness as college costs rose and federal aid fossilized, Congress last September passed The College Cost Reduction and Access Act, which provides an additional \$20 billion in student aid over the next five years. The act was heralded as a major improvement, but its impact on college access will be negligible. The law increases the maximum Pell Grant by about \$500 each year over the next five years, to \$5,400 in 2012. The act also creates an income-based repayment system that caps the amount student borrowers would pay on their loans to 15% of their discretionary income (any income above 150% of poverty, or about \$15,000 for a single individual). Finally, the law reduces the interest rate charged on certain new student loans, cutting it in half by 2012. These improvements are paid for by reducing the subsidies the government currently provides to student-loan companies. But none of these reforms is adequate to address the scale of the problem. The increases in the Pell Grant are likely to be underwhelming as college costs continue to increase, and the changes to student loan repayment options will help the most vulnerable and extreme cases of students with low earnings and high student debt, but will leave the overall system intact.

In a country where higher education serves as the primary lever of economic and social mobility, the debt-for-diploma system represents a major failure. It's predicted that over the next decade, millions of college-ready students will fall through the cracks of the current financial aid system. Their aspirations and our future hinge on whether or not bold action is taken now to restore the ladder of opportunity and end the failing debt-for-diploma system.

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